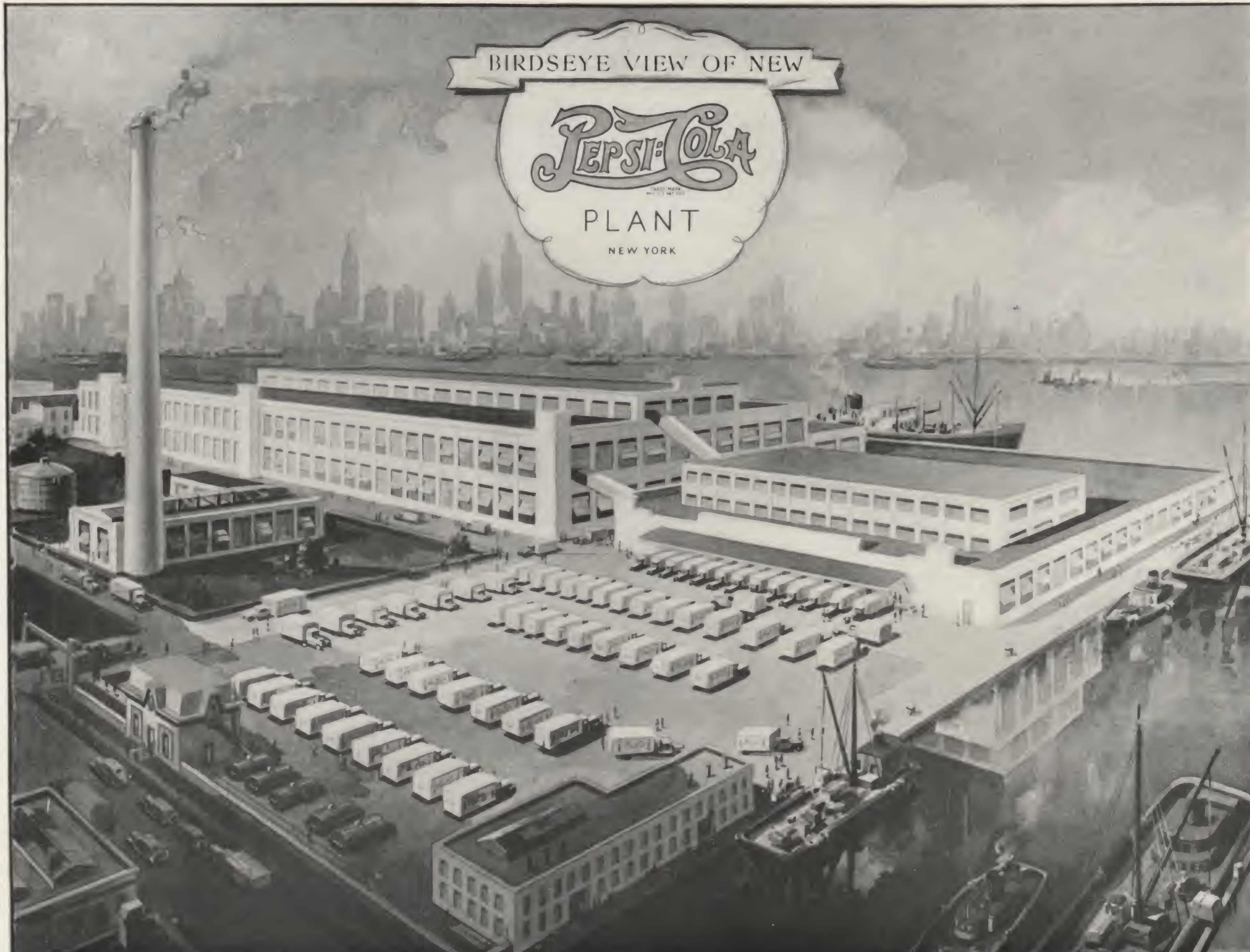
# PEPSI-COLA COMPANY

## ANNUAL REPORT

## 1939


BIRDSEYE VIEW OF NEW
PEPSI-COLA
PLANT
NEW YORK

# THE 1939 ANNUAL REPORT

OF

# THE PEPSI-COLA COMPANY

March 1st, 1940

*To Our Stockholders*:

This is the first Annual Report of the present management. I am, therefore, going into somewhat more detail than is customary in a President's letter to stockholders, in order to answer some of the numerous questions that I know are in the stockholders' minds. The drink itself, however, needs no discussion, as the popular demand and public approval of the flavor, taste and purity of Pepsi-Cola is long established and well-known.

## FINANCIAL REVIEW

There is presented herewith a review of the operations of your Company and Subsidiaries for the year 1939, together with a Consolidated Balance Sheet at December 31, 1939, and a Summary of Consolidated Income and Earned Surplus for the year then ended, certified by Haskins & Sells, independent certified public accountants.

## INCOME

The Consolidated Net Income after provisions for all taxes and all ordinary expenses, but before deduction of special settlement and legal expenses, was \$5,650,139.31 or approximately \$21.79 per share on the capital stock outstanding at December 31, 1939. This shows, on that basis, an improvement in Net Income for 1939 over the previous year of approximately 73%.

During the year 1939 the Company had some very sizeable expenditures in connection with the settlements of lawsuits, and other claims and expenses, which

due to their non-recurring nature have been grouped under the heading of Extraordinary Charges. These include the settlement made of the many claims and cross-claims and litigations involving Mr. Charles G. Guth et al., details of the settlement of which were sent out to all stockholders in June, 1939. This settlement was approved by the Court after a hearing before the Chancellor of the State of Delaware. In connection with these settlements payments were made and losses taken by the Company totalling $379,689.69. Also payment was made in settlement of the suit brought by Margery K. Megargel for the sum of $120,000.00. In addition thereto, there were extraordinary legal expenses in connection with these matters and other special litigation disposed of aggregating $279,970.80. After deducting from Income the above-mentioned non-recurring extraordinary payments, expenses, etc., totalling $779,660.49, the Net earnings, after such deduction, on the Capital Stock outstanding at December 31, 1939 were $18.78 per share.

The Net Income for each of the past four years, before deduction of special settlement and legal expenditures is as follows:

| | |
|---|---|
| 1936 | $1,544,110.61 |
| 1937 | $2,264,253.85 |
| 1938 | $3,266,457.16 |
| 1939 | $5,650,139.31 |

The Company paid a dividend of $15.00 a share on December 8, 1939, which aggregated $3,889,155.00. During the year the Company exercised its option under the settlement agreement to purchase 2,209 shares of the capital stock of this Company held by Mr. Charles G. Guth at $140.00 per share, thereby reducing the number of shares outstanding to 259,277.

## COMPANY'S PLANTS AND EQUIPMENT

The Company's Plants and Equipment are all in good shape. They have been reviewed and checked by the present management and a number of important changes in equipment have been made so as to increase facilities and improve their efficiency. A new extension is, at the present time, being built at the East River Bottling Plant which should be completed in a few weeks.

The Company, including its subsidiaries, operates the following plants:

(a) The East River Bottling Plant in Long Island City, which is considered to be the largest Bottling Plant under one roof in the world. A picture of this Plant appears on the back front cover. This Bottling Plant has a capacity to scour, fill, crown, label and pack over 2100 bottles *per*

*minute.* In order better to visualize the magnitude of this Plant's capacity, as an illustration it has three miles of conveyors running through it. The combined weight on an active summer day of bottles and cases loaded and unloaded at this plant is about 4,000,000 pounds.

(b) The Concentrate Plant at 47-51 33rd Street, Long Island City.
(c) The Newark, New Jersey, Bottling Plant.
(d) The New Brunswick, New Jersey, Bottling Plant.
(e) The Brooklyn, New York, Bottling Plant.
(f) The Boston, Mass. Bottling Plant, which is now under construction and should be in operation by the early Spring.
(g) The Philadelphia, Pa., Bottling Plant.
(h) The Pittsburgh, Pa., Bottling Plant.
(i) The Montreal, Canada, Bottling Plant.
(j) The Ottawa, Canada, Bottling Plant.
(k) The Winnipeg, Canada, Bottling Plant.
(l) The London, England, Bottling Plant.
(m) The Havana, Cuba, Bottling Plant.

In this connection I think it would be of interest to the stockholders to know that in our Long Island plants we manufacture,—in addition to the concentrate which is shipped to the franchise bottlers,—most of the other materials other than bottles that a franchise bottler needs in his operations. In these plants, which are modern and well equipped, we have a Crown Department with a capacity of manufacturing over 7,000,000 crowns *per day*; a Label-printing Department which has a capacity of printing over 5,000,000 sets of body and neck labels *per day*; and a Box Department, which manufactures the wooden cases for the bottles, and is reputed to be the largest box-manufacturing plant in the world under one roof, having a daily manufacturing capacity of more than 9,000 cases. A Pepsi-Cola case holds 24 bottles. These special Pepsi-Cola cases are made out of 100% cotton-wood, and take a total *daily* requirement of 1 and ½ tons of nails and 1 and ½ tons of strap iron.

Here, too, is the Grinding Plant where the large quantities of Cola nuts are ground. These Cola nuts are imported directly by us from the West Indies and Africa.

At the East River Plant, is the Pepsi-Cola Sugar Refinery, completed in 1939 and equipped with the most modern processing machinery. This plant refines its own sugar from raw sugar bought directly by us. The Refinery has a daily refining capacity of over 350,000 pounds of raw sugar and a storage capacity of over 23,000,000 pounds.

From the foregoing it is to be seen that the Pepsi-Cola Company is indeed practically a self-contained organization.

## GROWTH AND SCOPE OF OPERATIONS

In addition to the Company plants above enumerated, the Company has granted franchises to bottlers in the United States, Canada, West Indies, South America, Central America, Europe and Asia.

*United States*

As of December 31, 1939 your Company has granted franchises to more than 400 bottlers to bottle and distribute Pepsi-Cola in their territories. This compares with approximately 370 franchise bottlers as of December 31, 1938. The territories in which these bottlers distribute Pepsi-Cola include substantially all markets in the United States. I do not mean to imply that there are no open territories, but substantially all of the important cities and centers of population are now franchised. As a result of close contact and cooperation between the Management of the Pepsi-Cola Company and its franchise bottlers greatly improved results are being obtained by the parent Company and its bottlers. Meetings have been inaugurated by our Sales and Service Departments throughout the United States in order to help and guide the franchise bottlers in more thorough methods of distribution, advertising and service. Recently, Sales Schools have been inaugurated for the same purpose with excellent results.

Allow me to point out that there is still a lot of work to be done by ourselves and the franchise bottlers in bringing distribution in the United States to a point approximating where it should be. At the present time through the assistance of the parent Company to the franchise bottlers in establishing Sales Schools, Meetings, Advertising Campaigns and by the development of special Sales and Service crews, progress is being made towards obtaining satisfactory coverage in these territories. All of this, however, will take time.

*Canada*

The Canadian market is a large and fertile field. During the present year a plant has been opened at Winnipeg, Canada, in order better to service Western Canada. In addition to the Company plants as enumerated in the early part of this report, there are approximately 95 franchise bottlers in Canada, as compared with 85 on December 31, 1938. Canada, from the head Canadian Office in Montreal, is bringing the franchise bottlers and the General Canadian Office closer together in its efforts to help the franchise bottlers in their distribution and sales efforts with a program similar to that described in the United States.

*South America, Central America, West Indies, Africa and Asia*

A special program was recently inaugurated for the franchising of bottlers in the above territories and a new department for the development of these countries has been set up. This department is making considerable progress and a number of bottlers have already been franchised in a few of the important cities in these areas. It will take some time for these franchise bottlers to have their plants and equipment in operation and to be distributing Pepsi-Cola. It probably will be the latter part of this year or the early part of next year before the results of these new franchise bottlers and the development of this important market outside the United States will start to make itself felt.

*Europe*

The program that the Company had recently inaugurated for the development of franchise bottlers throughout Europe working from our wholly-owned subsidiary company, The Pepsi-Cola Company Ltd., in Great Britain has temporarily been held up due to the war. Economic and financial conditions throughout Europe being what they are at the present time it is believed that it is to the best interest of the Company that any special efforts in this direction be curtailed until the war is over.

## PEPSI-COLA'S CONTRIBUTION TO GENERAL BUSINESS IN THE UNITED STATES

I believe that few realize the breadth and scope of the operations of the Pepsi-Cola Company. Not only is its direct volume of business great but it affects in a large way almost every industry and trade, not only through the tremendous volume of purchases of supplies and materials of the parent Company but also through the volume of business of its franchise bottlers and their distributors on down to the millions of storekeepers and retail merchants themselves who are dependent in part on the sale of Pepsi-Cola for a living. In fact, it can be said that this is a business of the small business man.

The ramifications of this business are too numerous to go into great detail here, therefore I will only try and point out some of the most important items.

*Purchases*

The parent Company and its domestic subsidiaries for the year 1939 bought and paid for over $7,500,000 worth of materials and supplies. It used about 8,000,000 sheets of decorated tin plate; more than 2,000,000 pounds of kraft board; more than 1,300,000 pounds of chipboard. It purchased over 68,000,000 pounds of

raw sugar,—not to mention its enormous purchases of ingredients for the drink, bottles, automobiles, trucks, tires, fuel, bottling machinery, barrels, kegs, paper, refrigerators, etc., etc.

It has been estimated that the Pepsi-Cola franchise bottlers besides spent over $4,000,000 in the automobile industry in 1939, and the further amount that they spent with the hundreds of supply and allied industries runs into very sizeable figures but are far too numerous to list here. If we were to go further and point out the expenditures made by the distributors who work in conjunction with these Pepsi-Cola franchise bottlers and then estimate the contribution to business in the United States which their retail outlets made, you would be able to form a fair opinion of the ramifications and the effect that your Company has in almost every line of industry in almost every part of the United States.

*Employment*

The parent Company and its domestic subsidiaries paid out in salaries and wages, last year over $2,300,000. In addition to that it is estimated that our franchise bottlers throughout the United States spent another $16,000,000. But this is only part of the story. If one considers the number of distributors that each of our franchise bottlers has, who buy their merchandise directly from the bottler and sell it to the retailer, and the number of retailers that get employment by the profitable sale of Pepsi-Cola and other soft drinks to the consumer, the number of people who are dependent on this industry for a living is enormous.

*Taxes*

The parent Company and its domestic subsidiaries for 1939 will pay taxes of about $1,300,000. In addition to that are the taxes paid by the franchise bottlers throughout the United States and their wholesale distributors and retailers. From the foregoing it is to be seen that Pepsi-Cola's operations make a real contribution to the nation's tax rolls.

## MOVING FORWARD

Considerable progress has been and is being made to improve the management of the Company in order to get close and complete cooperation between the franchise bottlers, their men and the parent Company.

The Service Department of the Company is very active in studying and guiding the actual mechanical operations in the franchise bottlers' plants and helping to coordinate and standardize the machinery and equipment used throughout the

country. Under this Department standard colors for trucks, standard designs for signs and even, more recently, a standard bottle have been inaugurated. This Service Department is proving of considerable help in the mechanics of technical operations to all members of the Pepsi-Cola family.

A new Sales and Sales Promotion Department has been organized which is tackling the most important job of sales and distribution. The work in this field that remains to be done in helping our franchise bottlers get the necessary distribution in their territory is enormous. The results of this work which has been started will begin to be shown during the year 1940.

A new Advertising Department has recently been instituted, to cooperate with the Advertising Agency which was recently appointed in order to embark on a substantial National Advertising Campaign for the year 1940. In addition it is designed to guide and help the franchise bottlers in their local advertising problems, as well as to consult and service them with the necessary advertising media.

A new Purchasing Department has been instituted in order to reduce, as far as possible, the expenses of operation, and to coordinate and consolidate all purchases under one head.

The Company has recently established its own Legal Department, so that most of the routine legal matters can now be handled directly in its own offices.

These and many other things too numerous to include in this report have been organized and are being developed. The program is a most comprehensive one and the Officers of your Company are devoting time and a great deal of energy to putting these objectives in operation with the greatest despatch.

We look forward with confidence to the continued expansion and success of your Company.

Walter S. Mack, Jr.,
*President.*

## PEPSI-COLA

**(Incorporated**

**AND SUBS**

**CONSOLIDATED BALANCE**

### ASSETS

| | | |
|---|---|---|
| **Current Assets:** | | |
| Cash | $2,301,732.91 | |
| Notes receivable | 113,036.57 | |
| Accounts receivable | 79,961.87 | |
| Margin deposits against open sugar future contracts | 85,280.00 | |
| Inventories (at cost which is not in excess of market): | | |
| Finished and in-process inventories | 179,192.41 | |
| Raw materials and supplies | 1,228,829.96 | |
| Total Current Assets | | $3,988,033.72 |
| **Miscellaneous Assets:** | | |
| Notes and accounts receivable—not current (less reserve of $75,106.12) | $316,112.99 | |
| Machinery held for resale | 67,345.24 | |
| Other | 9,651.55 | |
| Total Miscellaneous Assets | | 393,109.78 |
| **Investments:** | | |
| Capital stock of Loft, Incorporated—11,700 shares at cost (market value $216,450.00) | $23,400.00 | |
| Other (less reserve of $31,116.36) | 13,763.24 | |
| Total Investments (Net) | | 37,163.24 |
| **Fixed Assets:** | | |
| Property, plant, and equipment (at cost) | $4,770,759.25 | |
| Less reserve for depreciation | 569,412.49 | |
| Remainder | $4,201,346.76 | |
| Bottles and cases on hand and with trade (at values as determined by officials of the companies which in the aggregate are less than cost) | 598,161.60 | |
| Total Fixed Assets (Net) | | 4,799,508.36 |
| **Trade-Marks, Formulas, and Goodwill** (at value determined by the Directors of the Company in 1931, representing the par value of 300,000 shares of capital stock issued therefor, of which 100,000 shares were donated back to the Company) | | 1,500,000.00 |
| **Deferred Debit Items:** | | |
| Prepaid insurance, taxes, etc. | $228,181.17 | |
| Advertising materials | 42,418.94 | |
| Leasehold improvements, less amortization | 38,355.91 | |
| Miscellaneous | 7,153.33 | |
| Total Deferred Debit Items | | 316,109.35 |
| **Total** | | $11,033,924.45 |

COMPANY

in Delaware)

IDIARIES

SHEET DECEMBER 31, 1939

LIABILITIES

| | | |
|---|---|---|
| **Current Liabilities:** | | |
| Accounts payable | $193,756.17 | |
| Accrued liabilities: | | |
| United States and Dominion of Canada income taxes (estimated) | 1,082,450.21 | |
| Other taxes | 221,051.77 | |
| Miscellaneous | 111,536.71 | |
| Total Current Liabilities (exclusive of customers' deposits on bottles and cases as stated in next item below) | | $1,608,794.86 |
| **Customers' Deposits on Bottles and Cases** | | 357,538.41 |
| **Capital Stock and Capital Surplus:** | | |
| Capital Stock: | | |
| Authorized and issued, 300,000 shares of $5.00 par value | $1,500,000.00 | |
| Less in treasury—40,723 shares | 203,615.00 | |
| Outstanding—259,277 shares | $1,296,385.00 | |
| Capital Surplus (representing the par value, $500,000.00, of 100,000 shares of Company's stock donated to the Company, less discount of $250,713.51 upon sale of 62,500 shares of such stock, plus net discount of $2,962.00 on 1,014 shares of Company's stock purchased) | 252,248.49 | 1,548,633.49 |
| **Earned Surplus** | | 7,518,957.69 |
| **Total** | | $11,033,924.45 |

The notes on the next pages following, including the references to contingent liabilities, are an integral part of the above statement and should be considered in connection therewith.

## PEPSI-COLA COMPANY AND SUBSIDIARIES

### NOTES TO CONSOLIDATED BALANCE SHEET
### DECEMBER 31, 1939

A. The consolidated balance sheet includes assets and liabilities of the Canadian, Cuban and British subsidiaries. Their current assets and liabilities have been converted into U. S. dollars at current rates of exchange as of December 31, 1939; their other assets and liabilities have been included herein at amounts which reflect their approximate U. S. dollar equivalent at the time of acquisition.

B. The Company has contingent liabilities as of December 31, 1939, as follows:

(1) Contingent liability arising out of the use of its trade-mark in connection with the manufacture, sale and distribution of its product in the United States and foreign countries.

(2) Pending litigation involved in trade-marks:

(a) Proceeding for an injunction and an accounting brought by The Coca-Cola Company of Canada, Limited vs. Pepsi-Cola Company of Canada, Limited, based upon an alleged infringement of the alleged Coca-Cola trade-mark, in which a decision was rendered in favor of the Pepsi-Cola Company of Canada, Limited, by the Supreme Court of Canada on December 9, 1939. (The Company has been advised that the plaintiff in this action intends to apply for permission to appeal to Privy Council in London, England.)

(b) Suit brought by the Pepsi-Cola Company vs. The Coca-Cola Company, seeking damages and injunctive relief restraining the latter company from engaging in certain alleged unfair business practices and activities. The Coca-Cola Company has interposed a counterclaim in this suit, charging unfair trade practices and infringement of its alleged trade-mark and seeking injunctive and accounting relief against the Pepsi-Cola Company. This proceeding is still pending in the Supreme Court of the State of New York, County of Queens.

(c) Litigations involving registration of the Pepsi-Cola trade-mark in various foreign countries.

(3) Other pending litigations:

(a) A petition in bankruptcy of the National Pepsi-Cola Corporation (a corporation which was adjudicated a bankrupt on June 8, 1931 in the

United States District Court, Eastern District of Virginia) by an alleged stockholder of that corporation, seeking, among other things, to set aside the conveyance by the Trustee in Bankruptcy of that corporation of the trade-marks, formulas, patents, goodwill, personal property, etc. to Roy C. Megargel, who subsequently made assignments thereof to the Pepsi-Cola Company. A decision dismissing said petition was rendered by the United States District Court in the Eastern District of Virginia on December 6, 1939. Subsequent thereto a notice of appeal was served by said petitioner.

(b) Suit by Elizabeth L. Megargel, administratrix of the estate of Ralph G. Megargel against Pepsi-Cola Company, Loft, Incorporated and Charles G. Guth, involving alleged ownership of 2500 shares of stock of the Pepsi-Cola Company. This action is based upon the alleged claim that Ralph G. Megargel, the alleged owner of said shares, was induced by fraudulent representations to contribute said shares in order to consummate the settlement in 1933 of the claims of his brother Roy C. Megargel against Pepsi-Cola Company and Charles G. Guth. This action has just been instituted in the Supreme Court of the State of New York, County of New York, and as yet no answer has been interposed.

(c) Various other claims against Pepsi-Cola Company and its subsidiaries aggregating not in excess of $50,000.00.

(4) The claim of an attorney for $100,000.00 for alleged services in connection with the settlement of the case "Loft, Incorporated vs. Charles G. Guth, et al.".

The Company admits no liability in connection with all of the above suits and claims and no provision for loss in connection therewith has been made in the accompanying statements.

(5) In addition to the suits listed above under contingent liabilities, there was pending at December 31, 1939 in the Court of Chancery, State of Delaware, an application by Bartus Trew, a stockholder of the Pepsi-Cola Company, for leave to intervene in the suit of Loft, Incorporated vs. Charles G. Guth, et al., for the purpose of asserting on behalf of the Pepsi-Cola Company claims to certain of the Pepsi-Cola stock awarded to Loft in that litigation.

## PEPSI-COLA COMPANY AND SUBSIDIARIES

### SUMMARY OF CONSOLIDATED INCOME AND EARNED SURPLUS
### FOR THE YEAR ENDED DECEMBER 31, 1939

| | | |
|---|---|---|
| Gross Profit on Sales | | $11,269,128.14 |
| Selling, General, and Administrative Expenses | | 4,490,569.26 |
| Profit From Operations | | $6,778,558.88 |
| Other Income: | | |
| Interest received | $4,441.20 | |
| Rent | 7,141.67 | |
| Miscellaneous | 17,921.40 | |
| Total | | 29,504.27 |
| Gross Income | | $6,808,063.15 |
| Income Charges: | | |
| Provision for United States and Dominion of Canada income taxes | $1,075,600.07 | |
| Loss on sale or abandonment of equipment, etc. | 14,623.43 | |
| Loss on foreign exchange conversion | 46,201.13 | |
| Miscellaneous | 21,499.21 | |
| Total | | 1,157,923.84 |
| Net Income (before deducting extraordinary charges in connection with settlements and special litigation) | | $5,650,139.31 |
| Deduct: | | |
| Payments, losses, etc., in connection with settlement of the case "Loft, Incorporated vs. Charles G. Guth, et al." | $379,689.69 | |
| Payment in settlement of Margery K. Megargel suit | 120,000.00 | |
| Extraordinary legal expenses | 279,970.80 | |
| Total | | 779,660.49 |
| Net Income (after deducting the foregoing extraordinary charges) | | $4,870,478.82 |
| Earned Surplus, January 1, 1939 | | 6,835,848.87 |
| Gross Earned Surplus | | $11,706,327.69 |
| Surplus Charges: | | |
| Dividends paid | $3,889,155.00 | |
| Excess of cost of 2,209 shares of Company's stock purchased over the par value thereof (acquired in pursuance of an option granted in the settlement with Charles G. Guth, et al.) | 298,215.00 | |
| Total | | 4,187,370.00 |
| Earned Surplus, December 31, 1939 | | $7,518,957.69 |

Notes:

(a) Depreciation included in cost of sales and selling, general, and administrative expenses amounts to $360,900.95.

(b) The net income from operations in foreign countries, except as to provision for depreciation and loss on sale of fixed assets, has been converted into U. S. dollars at monthly average quoted rates of exchange.

HASKINS & SELLS
CERTIFIED PUBLIC ACCOUNTANTS

67 BROAD STREET
NEW YORK

## ACCOUNTANTS' CERTIFICATE

PEPSI-COLA COMPANY:

We have examined the consolidated balance sheet of Pepsi-Cola Company and its subsidiary companies as of December 31, 1939 and the summary of consolidated income and earned surplus for the year ended that date, and, as to companies other than the British and Canadian subsidiaries, have reviewed the system of internal control and the accounting procedures of the companies and have examined or tested their accounting records and other supporting evidence by methods and to the extent we deemed appropriate. As to the British and Canadian subsidiaries, we have examined reports of chartered accountants, and the figures included in the accompanying statements with respect to such subsidiaries are derived from such reports. The total assets of these subsidiaries amount to approximately 12% of the consolidated total, and their gross profit on sales and net income aggregate approximately 10% and 11% respectively of the consolidated totals.

In our opinion, which as to the British and Canadian subsidiaries is based upon the reports of chartered accountants, the accompanying consolidated balance sheet and the related summary of consolidated income and earned surplus, with the footnotes thereon, fairly present the financial condition of Pepsi-Cola Company and its subsidiary companies at December 31, 1939 and the results of their operations for the year ended that date, in conformity with generally accepted accounting principles followed by the companies on a basis consistent with that of the preceding year.

New York,
March 1, 1940.

HASKINS & SELLS

## DIRECTORS

| | |
|---|---|
| Frank P. Burns | Walter S. Mack, Jr. |
| James W. Carkner | Herman Shulman |
| Edward A. Le Roy, Jr. | Harral S. Tenney |

Arthur T. Vanderbilt

## OFFICERS

Walter S. Mack, Jr. ........................ *President*

Don G. Mitchell ..................... *Vice-President*

J. Willard Pipes ..................... *Vice-President*

Phillip C. Crowen ..................... *Vice-President*

Milward W. Martin ...................... *Secretary*

J. A. Murphy ............................ *Treasurer*

R. V. Faragher ..................... *Asst. Secretary*

## AUDITORS

Haskins & Sells
Certified Public Accountants

## TRANSFER AGENT

The Marine Midland Trust Company of New York
120 Broadway, New York

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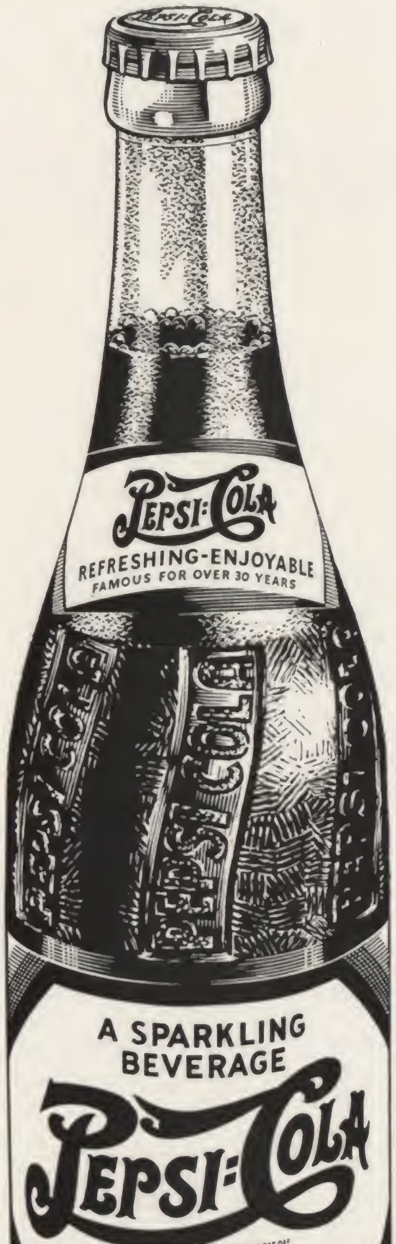
PEPSI-COLA
REFRESHING-ENJOYABLE
FAMOUS FOR OVER 30 YEARS
A SPARKLING
BEVERAGE
PEPSI-COLA
REFRESHING-SATISFYING
12 OUNCES